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39. In addition, agreements that disclose the valuation method, without elaboration, are insufficient to meet the requirements of section 272(b)(5), because again such disclosure is too meager to evaluate compliance with the accounting rules, as required.²⁰ Instead, the disclosure of the valuation method should include additional information necessary to evaluate whether the particular method is appropriate for the particular transaction, and to determine whether the valuation method used appropriate systems, estimates, and assumptions.²¹

40. Also, the "rates" listed for at least two of the BellSouth/BSLD agreements on their face do not comply with the Commission's accounting rules. These agreements -- the Trial Marketing and Sales Agreement, and the BellSouth Telecommunications Fraud Management Services Market Trial Agreement -- contain pricing provisions stating that the rates listed are subject to change following a "cost analysis" or a "comprehensive business analysis," at which time the rates will be reset to represent a "fair market value" that "will be deemed by [BellSouth] to be appropriate for federal regulatory accounting rule compliance." Trial Marketing and Sales

²⁰ For example, the Workbrief Agreements Regarding AIN Applications, Amendment.3., identifies the valuation method as fully distributed costs, without providing any detail as to the systems or assumptions used to reach these costs. Wentworth Aff., Exh. 4. Similarly, the Trial Marketing and Sales Agreement, Schedule A.4., asserts that fair market value will be used in setting rates, without elaborating on how that value will be calculated. Wentworth Aff., Exh. 4.

²¹ For example, if a tariff is stated as the valuation method, then the disclosure should include a citation to the particular tariff relied upon. If the method of valuation is fully distributed costs, then the disclosure should include information as to the systems used to calculate the fully distributed costs as well as the key assumptions made. Providing such information will impose no undue burden on BellSouth, which already gathers precisely this information under its internal affiliate transaction procedures. See Cochran Aff. Exh. V (BellSouth Corporate Policy on Affiliate Transactions).

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Agreement, Schedule A, 4.1; BellSouth Telecommunications Fraud Management Services Market Trial Agreement, 5 (Rates and Settlement). These provisions thus acknowledge that the current rates for those agreements have not been based on any valid evaluation of a fair market value, and thus cannot meet the requirements of the Accounting Safeguards Order, ¶¶ 125-159 (delineating appropriate valuation methods).²²

41. Finally, BellSouth's own application shows the reasonableness of requiring that it provide the detailed information regarding each individual transaction required by section 272(b)(5), as called for above. BellSouth's current policy on affiliate transactions, as reflected by Exhibit V of the Cochran Affidavit, requires that documentation for affiliate transactions "should include as a minimum" a "[c]omplete description of proposed contract(s) and/or transaction(s) including frequency, magnitude, pricing methodology, etc.," and should demonstrate that the appropriate valuation method was used, including, if applicable, a "method of estimation and key assumptions made." BellSouth, therefore, already gathers the very type of information it is required to disclose under section 272(b)(5). See Cochran Aff. Exh. V (BellSouth Corporate Policy on Affiliate Transactions).

²² These contract provisions vaguely provide for a "true up" following this resetting of rates "if necessary," but only if both parties agree to a "final price." See Trial Marketing and Sales Agreement, Schedule A, 4.1; BellSouth Telecommunications Fraud Management Services Market Trial Agreement, 5 (Rates and Settlement). It thus is unclear whether such a true up is required under these agreements, or merely permissible. Moreover, these true-up provisions do not provide for any interest to be paid based on prior underpayments by BSLD.

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C. **The Need For Full Disclosure Of The Details Of All Transactions Between BellSouth And BSLD Is Shown By The Collocation Agreement, Which Is Discriminatory On Its Face.**

42. The disclosure obligations imposed by section 272(b)(5) and the Accounting Safeguards Order act both to facilitate oversight of BellSouth's compliance with the Act and also to deter discriminatory transactions in the first place because of the increased threat of detection. The need for full disclosure of the details of all transactions is shown starkly in the present application by the BellSouth/BSLD collocation agreement, which is discriminatory on its face. See Wentworth Aff., LAW Exh. 4, BellSouth Physical Collocation Master Agreement ("BSLD Collocation Agreement").

43. This BSLD Collocation Agreement provides BSLD with the "right to occupy" certain identified space "within a BellSouth Central Office." BSLD Collocation Agreement I.A. The term provision in the BellSouth/BSLD collocation agreement provides that the agreement "shall be for an initial term of two (2) years," beginning on the date BSLD's "equipment becomes operational." BSLD Collocation Agreement II.A (emphasis added). In contrast, the collocation agreement that BSLD is offering generally to CLECs provides that the agreement runs for a period of two years "beginning on the Agreement date." Tipton Aff., PAT Exh. 1, BellSouth Physical Collocation Master Agreement ("CLEC Collocation Agreement") 1.6. Thus, although BellSouth and BSLD entered into the BSLD Collocation on June 5, 1997, the two-year term of the agreement does not begin to run until BSLD actually places operational equipment in the collocated space. Had BSLD been made subject to the

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term provision in the CLEC Collocation Agreement, the two-year term would conclude less than one year from today, on June 5, 1999.

44. In addition, both the BSLD Collocation Agreement and the CLEC Collocation Agreement provide that operational equipment must be placed in the collocation space within 180 days from the date that BellSouth notifies the interconnector that the collocation space "is ready for occupancy." BSLD Collocation Agreement II.B.; CLEC Collocation Agreement 2.2. However, the BSLD Collocation Agreement also provides that "BellSouth may consent to an extension beyond 180 days upon a demonstration by Interconnector that circumstances beyond its reasonable control prevented Interconnector from completing installation by the prescribed date." BSLD Collocation Agreement II.B. The CLEC Collocation Agreement contains no such consent provision.

45. The BSLD Collocation Agreement, therefore, provides BSLD the opportunity to reserve collocation space indefinitely, as long as it receives the consent from BellSouth to extend the date upon which it must place equipment in the collocated space.²³ CLECs, however, are provided no such opportunity under the CLEC Collocation Agreement.

46. The BSLD Collocation Agreement thus on its face provides terms that are more favorable than those offered by BellSouth in the CLEC Collocation Agreement. BellSouth

²³ Furthermore, BellSouth may delay starting the two-year contract period by merely not "releas[ing] the collocation space for occupancy" to BSLD. BSLD Collocation Agreement, V(B). Until BellSouth releases this space, BSLD neither pays any monthly charges for the collocation space, nor does its two year agreement begin to run. *Id.* at II(A and B), V(B).

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has made no attempt to justify or explain the different treatment provided under these agreements to its affiliate and its competitors.

D. BellSouth And BSLD Have Failed To Comply With The Internet Posting Requirements Under The Accounting Safeguards Order.

47. Besides failing to provide the required information regarding each of their transactions, BellSouth and BSLD also have failed to meet the timing requirements for such disclosure on the Internet. As noted above, the Accounting Safeguards Order requires that all transactions between the BOC and Section 272 affiliate be posted "on the Internet within ten days of the transaction." Accounting Safeguards Order, ¶ 122. This posting requirement has been known to the BOCs since December 24, 1996 (when the Order was issued), and became effective on August 12, 1997. See Accounting Safeguard Rule Changes Requiring OMB Approval Soon to be Effective, Public Notice, DA 97-1669 (released Aug. 5, 1997). Yet many substantial transactions between BellSouth and BSLD occurring after August 12, 1997 were not reflected in the BellSouth Internet site until after the present application was filed on July 9, 1998, more than six months after these transactions were completed.

48. For example, the Wentworth Affidavit identifies six categories of "past transactions" occurring from September, 1997 through November, 1997, for which BellSouth billed BSLD a total of \$923,700.²⁴ BellSouth and BSLD provided no information on the Internet

²⁴ BellSouth's current disclosures, when compared with its past disclosures, show that it billed BSLD \$399,500 for "Customer Billing Services" provided from September, 1997 through November, 1997, \$217,900 for "Information Technology - Billing Systems" provided from September, 1997 through November, 1997, and \$207,100 for "Sales Channel Planning and Design" provided from September, 1997 through October, 1997, \$71,900 for "Project

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site regarding these transactions, however, until sometime after July 10, 1998 (at least one day after the present application was filed).²⁵ Over six months passed after these transactions were completed, therefore, before BellSouth and BSLD provided any information on the Internet site regarding these transactions (which disclosure, as discussed above, ¶¶ 25-32, is itself wholly unsatisfactory). At the very least, this experience shows that BellSouth and BSLD have wholly inadequate procedures in place to assure that the 10-day rule in the Accounting Safeguards Order is met.²⁶

²⁴ (...continued)

Management provided from September, 1997 through October, 1997, 11,100 for "Investment Related Costs - PCs provided from September 1997 through November 1997, and \$16,200 for "Mail Service" provided from September, 1997 through October, 1997. I have obtained these billing figures by comparing the information currently available on BellSouth's Internet site for "Past Transactions" with the information available under the heading "Past Transactions" that was available on the Internet site as of July 10, 1998.

²⁵ I have attached a copy of the relevant section of BellSouth's Internet site that was printed on July 10, 1998, which reflects the fact that as of that date no information had been provided regarding these transactions. Similarly, although the Wentworth Affidavit identifies services for "Library Research" in 1997, the Internet site as of July 10, 1998 contained no mention of these services. BellSouth has since amended the Internet site so that it contains the same information as is found in the Wentworth affidavit regarding "past transactions."

²⁶ In addition, a comparison of the execution dates of certain now-disclosed agreements (all entered into after August 1997) with an ex parte submission to the Commission by BellSouth of a copy of its Internet site in March 1998, reveals that BellSouth has waited months, not days, before posting its transactions with BSLD. For example, Amendment 7 to the End to End Test Agreement -- Interexchange Transport Service, although executed in January 1998, was not posted on BellSouth's Internet site by March 1998. Similarly, Amendment 3 to the End to End Test Agreement - InterLATA Toll, which was entered into on December 17, 1997, was not posted on BellSouth's Internet site by March 1998. I am unaware when these transactions eventually were posted on the Internet site.

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49. Moreover, because no information is provided on BellSouth's Internet site concerning the dates of transactions under the various agreements, it is impossible to evaluate whether any of this information was posted in a timely fashion. On this record, BellSouth and BSLD cannot meet their burden of establishing that they will operate in compliance with the Internet posting requirements.

50. There also is substantial reason to doubt the accuracy of the transaction information currently disclosed on the Internet site. The posted agreements differ in significant respects from similar agreements made available for public review by BellSouth at its place of business.²⁷ In addition, four categories of transactions listed as "past transactions" on the Internet site as of July 10, 1998, have been dropped from the current listing of "past transactions" on the Internet site. The prior listing indicated that the value of these four transactions was \$2,415,609.²⁸ BellSouth and BSLD have provided no explanation of any kind for its deletion of these prior postings.

²⁷ On July 21, 1998, I reviewed all the documents made publicly available by BellSouth at its Atlanta offices. Two of the agreements made available for my review -- the End to End Test Agreement - Interexchange Transport Service and the End to End Test Agreement - IntraLATA Toll -- did not include amendments that appear in the corresponding agreements submitted with this application and posted on the Internet.

²⁸ The four categories of "past transactions" that no longer appear on the Internet site are Interoffice Testing - CO Switch (with total billings of \$42,800), Telecommunications Services (with total billings of \$166,500), End to end testing (with total billings of \$2,309), and Collocation (with total billings of \$2,204,000). The printout for the Internet site as of July 10, 1998 is attached as Attachment 1 to my affidavit.

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E. BellSouth And BSLD Have Not Presented Information Sufficient To Justify Their Decision Not To Disclose Any Transactions Between BSLD And Other BellSouth Affiliates.

51. BellSouth and BSLD have not disclosed details of any transactions between BSLD and other BellSouth affiliates. This Commission repeatedly has stressed, however, that "a BOC cannot circumvent the Section 272 requirements by transferring local exchange and exchange access facilities and capabilities to an affiliate."²⁹ Moreover, it is clear that Section 272 obligations govern "chain transactions" where an unregulated affiliate stands between the BOC and the Section 272 affiliate in the provision of assets, information, or services. See Accounting Safeguards Order ¶ 183. Before they can meet their burden regarding Section 272 under the Act, therefore, BellSouth and BSLD must disclose sufficient information regarding transactions between BSLD and other affiliates to support their apparent position that these transactions are not subject to the disclosure and nondiscrimination obligations of Section 272. BellSouth and BSLD have not even attempted to make such a showing in this application.

52. This Commission was faced with a similar lack of disclosure in Ameritech Michigan's application for interLATA authority last year. In response, the Commission again made plain "that, 'if a BOC transfers to an affiliated entity ownership of any network elements that must be provided on an unbundled basis pursuant to Section 251(c)(3), we will deem such entity to be an "assign" of the BOC under Section 3(4) of the Act with respect to those network elements. Any successor or assign of the BOC is subject to the Section 272 requirements in the same manner as the BOC.'" Ameritech Michigan Order ¶ 373 (quoting Non-Accounting

²⁹ Non-Accounting Safeguards Order ¶ 309; Ameritech Michigan Order ¶ 373.

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Safeguards Order, ¶ 309). The Commission then found that Ameritech had not submitted "adequate information" to allow the FCC "to determine whether Ameritech has transferred local exchange and exchange access facilities and capabilities to [its other affiliates]." The Commission concluded by instructing Ameritech, in any future Section 271 application, to submit information sufficient to allow such a determination to be made. Ameritech Michigan Order ¶ 373.

53. BellSouth and BSLD have presented absolutely no evidence to support their decision not to disclose any details of past, current, or anticipated transactions between BSLD and other affiliates. On this record, no judgement can be made as to whether any such transactions are subject to the requirements of Section 272. At the very least, BellSouth and BSLD must disclose the nature, timing, and subject matter of all such past transactions and anticipated future transactions. At minimum, this information must be sufficiently detailed to allow this Commission to evaluate whether the transactions involve network elements subject to Section 251(c)(3) that were transferred to the affiliates or whether the transactions otherwise are "chain transactions" subject to each of Section 272's requirements.

V. BELLSOUTH HAS NOT PRESENTED EVIDENCE THAT IT HAS SUFFICIENT PROCEDURES OR SYSTEMS IN PLACE TO PROTECT AGAINST VIOLATIONS OF SECTION 272.

54. The Telecommunications Act has required BellSouth to change the way it does business. Section 272 itself presents a series of new obligations, requiring that BellSouth operate independently of, and at arm's length from, an affiliate created to provide interLATA services, publicly disclose the details of its transactions with this affiliate, and not provide services,

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information, or facilities to that affiliate on terms any more favorable than those provided to competitors of BellSouth.

55. In the face of these types of significant changes in the way business must be done, basic accounting principles require that BellSouth create new internal systems and procedures to protect against violations of its new legal obligations. Although BellSouth promises compliance with Section 272, it has failed to identify sufficient new procedures or systems that it has put in place and actively employs to respond to the new obligations it faces.

56. Without evidence of significant internal systems or procedures geared to section 272 compliance, there is no basis to conclude that BellSouth is ready and able to comply with section 272. These systems and procedures must address the following compliance problems, among others, raised in the context of section 272:

(i) BSLD's workforce includes a significant number of employees who formerly worked at BellSouth (although BellSouth is silent on the precise number of former BellSouth employees now at BSLD³⁰) These BSLD employees will have both the incentive and the ability to seek and obtain favorable treatment from their former coworkers at BellSouth, which obviously would be impermissible under section 272.

(ii) BSLD and BellSouth employees will have an incentive to engage in "off-the-record" transactions, especially concerning proprietary information such as

³⁰ In its brief, BellSouth vaguely states, without detail or citation, that "less than 1/3 are former employees of a local telephone company." (BellSouth Br. at 67).

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CPNI. Such "off-the-record" transactions will be especially difficult to identify and evaluate through any internal or external audit.

(iii) BSLD employees formerly employed by BellSouth have an incentive to take with them, and use, BellSouth proprietary information without accounting for this acquisition of information and without offering this information to competitors.

(iv) BSLD and BellSouth will have a strong incentive to share employee services on an ad hoc basis without properly accounting for such services.

57. The likelihood of such ongoing problems is shown starkly in BellSouth's application. In materials attached to the Betz Affidavit, in an April, 9, 1997, newsletter titled "Competitive Alert," BellSouth states: "There are recent situations where former employees of BellSouth -- who are now employed by our competitors -- have contacted BellSouth employees requesting special attention for service orders for their company. In many cases BellSouth employees have acted on behalf of these former employees and worked to grant these requests." Betz Aff., Exh. DMB-3. The frequency of such favorable treatment to former employees will inevitably increase where the former employees do not work for a competitor of BellSouth, but rather for a BellSouth affiliate that is viewed as part of BellSouth's corporate family.

58. The compliance problems identified above cannot be solved simply by sending materials to employees encouraging them not to engage in such discriminatory conduct in favor of their affiliate. Instead, compliance programs that place procedural impediments to such discriminatory conduct are needed.

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59. The type of compliance programs instituted by other BOCs with which I am familiar include procedures requiring that all transactions between a BOC and its section 272 affiliate be reviewed by an oversight committee to confirm its compliance with section 272. In this way the BOC can separate the process of evaluating section 272 compliance from the employees who are most interested in seeing the transaction completed. In addition, at least one BOC has stated its intent to require that all transactions proceed through specified customer contact points, which can help to ensure that affiliates, CLECs, and IXC's each receive the same access to BOC facilities, information, and services, and which protects against ad hoc "off-the-record" transactions.

60. I view compliance programs such as these, which are specifically geared to the unique obligations posed by section 272, as a prerequisite for a BOC to establish that it is ready and able to comply with section 272. Other than providing employees with training materials concerning section 272 obligations, see, e.g., Betz Aff. ¶¶ 4-7, BellSouth has not identified internal systems or procedures that it has instituted specifically to address the requirements of section 272 and to attempt to protect against violations of section 272. BellSouth's failure to present any tangible evidence of its implementation of such programs, despite having engaged in substantial ongoing transactions with BSLD, shows that it is not prepared to provide interLATA service in compliance with section 272.

61. For example, BellSouth's affidavits refer generally to internal audits that have been conducted (without identifying the specific purposes of these audits, the procedures followed, or their results), and appear to suggest that these internal audits will continue and will

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protect against violations of section 272. Cochran Aff., ¶ 26. But for such internal audits to be effective in identifying violations of section 272, auditing procedures must be revised to include methods specifically designed to seek out and evaluate transactions for assets, services and information that were not recorded or subject to a written agreement. No reliable or accurate evaluation of section 272 compliance can be made without identifying (or confirming the non-existence of) unrecorded transactions, because it is just such unrecorded dealings that provide the most ready means by which BellSouth and BSLD could engage in unfair cross-subsidization or other anticompetitive activities. BellSouth provides no specific evidence to show that its auditing program has been revised to address this unique compliance issue raised by section 272.

62. Moreover, BellSouth's assertion that its "existing accounting policies and procedures have proven effective over the year for ensuring compliance," Cochran Aff. ¶ 26, ignores the substantial criticism that BellSouth faced from past joint federal and state auditors, who found BellSouth to have engaged in a "consistent pattern of obstructionist behavior" regarding efforts by auditors to determine whether BellSouth improperly subsidized affiliates and who found numerous apparent violations by BellSouth of accounting rules and reporting requirements.³¹

63. The inadequacy of BellSouth's existing internal oversight procedures is further shown by its acknowledged past misuse of customer proprietary network information ("CPNI"). BellSouth states that, prior to switching the service of its customers who had selected a different local exchange carrier, it sent letters asking them to return to BellSouth's local service.

³¹ See infra ¶¶ 69-74.

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Varner Aff., ¶ 257 at 94. For a period from March 1997 to August 1997, these letters were sent to all business and residential customers who had asked to switch to a competitor's service. Id. BellSouth states that these letters mistakenly were sent as a result of a "programming change," yet it did not catch this error for approximately six months. Id. Plainly, whatever internal oversight systems BellSouth had in place as recently as this past summer were ineffective in identifying and correcting this serious error.³²

VI. BELLSOUTH AND BSLD HAVE NOT PRESENTED ANY PLAN TO IDENTIFY AND CORRECT PAST DISCRIMINATION OR SUBSIDIZATION.

64. When a BOC elects to provide in-region interLATA service through a pre-existing affiliate, as BellSouth has done, the BOC must present evidence to detail how it will identify, end, and correct, through a "true-up" or otherwise, all improper cross-subsidization and discrimination that may already have occurred prior to its application. The risk that such inappropriate subsidization or discrimination has occurred is substantial in this case, because BellSouth has admitted engaging in numerous transactions with BSLD and has stated that it has been operating to date under the view that none of the transactions between it and BSLD have been subject to the restrictions of section 272 or the Accounting Safeguards Order. See supra ¶ 9 & n.5.

³² The failure to identify this error in a timely fashion is made all the more egregious by the fact that, in May, 1997, AT&T contacted BellSouth and objected to BellSouth's practice of sending such marketing letters to customers that had switched to AT&T service. AT&T asked that BellSouth discontinue this practice, explaining that BellSouth was "using 'requests to switch' to impermissibly market AT&T customers." Letter from William Carroll, AT&T, to Charlie Coe, BellSouth, dated May 15, 1997. A copy of this letter is attached to this affidavit as Attachment 2.

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65. The Texas Commission and the staff of the California Commission both have recently acknowledged this need for BOCs and their section 272 affiliates to identify and true up past transactions that otherwise would provide the affiliate with unfair, anticompetitive advantages as it entered the long-distance market.³³ (I have attached to this affidavit the relevant portions of the Texas Commission's decision and the staff report of the California PUC as Attachments 3 and 4, respectively.) BellSouth, however, has not presented any evidence that it has established procedures to identify and correct any transactions that are not in compliance with section 272 and the Accounting Safeguards Order.³⁴ Unless BellSouth is called upon to identify and rectify any such past impermissible subsidies or transactions, BSLD would be able to enter the interLATA market with the very anticompetitive advantages that section 272 was designed to prevent. BellSouth has not even attempted to make such a showing.

³³ Investigation of Southwestern Bell Telephone Company's Entry Into The Texas InterLATA Telecommunications Market, Texas PUC, No. 16251, Commission Recommendation, at 16 (June 2, 1998) ("Transactions between February 1996 and the date of approval to initiate interLATA services shall be disclosed and made subject to 'true-up.'"); Pacific Bell (U 1001 C) and Pacific Bell Communications Notice of Intent to File Section 271 Application For InterLATA Authority in California, Calif. PUC, Initial Staff Report, at 74 (July 10, 1998) ("If considered appropriate by staff, said transactions between February 1996 and the date of approval to initiate interLATA services shall be disclosed and made subject to 'true up.'").

³⁴ Even under BellSouth's incorrect view that it does not need to comply with section 272 until it receives interLATA authority, it currently must have procedures in place to identify and correct transactions that are not in compliance with section 272 and the Accounting Safeguards Order. Because BellSouth has not presented any evidence of such procedures, BellSouth has failed to meet its burden of proving that it will be in compliance with section 272 once it receives interLATA authority.

VII. BELLSOUTH AND BSLD HAVE NOT SHOWN THAT THEY HAVE TRULY SEPARATE OFFICERS, DIRECTORS AND EMPLOYEES WHO WILL OPERATE THE 272 AFFILIATE INDEPENDENTLY AS REQUIRED BY SECTION 272(B)(3) OF THE ACT

66. Section 272(b)(3) requires that the Section 272 affiliate "have separate officers, directors, and employees from the [BOC] of which it is an affiliate." The Ameritech Michigan Order held that this requirement is breached where the officers of the BOC and Section 272 affiliate both ultimately reported, as a practical matter, not to their own independent board but instead directly to officers of the parent corporation. See Ameritech Michigan Order ¶¶ 353-362. This Commission thus made plain that the independence of a Section 272 affiliate is compromised when its officers report not to the its own board, but to officers of a parent company or affiliate who also have direct supervising responsibility for the BOC. See Ameritech Michigan Order, ¶ 362.³⁵

67. The information submitted by BellSouth and BSLD is insufficient to meet their burden under Section 272(b)(3). The only evidence presented by BellSouth and BSLD of their compliance with this requirement is the listing of their current boards of directors and the simple pledge not to share officers, directors, or employees. See Cochran Aff. ¶¶ 18-19; Wentworth Aff. ¶12 at 6.³⁶ Neither BellSouth nor BSLD have presented any information,

³⁵ "Given that the principal corporate officers of Ameritech Michigan and ACI [the 272 affiliate] report to the same Ameritech Corporation officer, it is clear that as a practical matter (as well as a matter of law), Ameritech Corporation is the corporate director for both Ameritech and ACI." Ameritech Michigan Order ¶ 362.

³⁶ It is noteworthy that BellSouth and BSLD do not assert that they have never in the past shared directors, officers, or employees. See Cochran Aff. ¶ 18 ("None of these persons is currently an officer or director of BSLD."); Wentworth Aff. ¶ 12 ("No officer, director, or

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however, regarding the reporting structure for their officers and employees. Without such information, it is impossible to determine whether, as a practical matter, the officers of BellSouth and BSLD report, not to an independent board, but rather to officers within their parent corporation, or other affiliate, who have direct responsibilities overseeing the operation of both BellSouth and BSLD.

68. Before BellSouth and BSLD can begin to meet their burden under Section 272(b)(3), therefore, they must establish that their officers and directors do not, as a practical matter, have reporting responsibilities that compromise the requirement under Section 272(b)(3) that they each operate independently under the direction of separate and independent boards. BellSouth and BSLD have not even attempted to make such a showing, and the thus cannot properly be found to have established compliance with Section 272(b)(3).

VIII. BELL SOUTH'S COMPLIANCE HISTORY PROVIDES A SUBSTANTIAL BASIS TO DOUBT BELL SOUTH'S PAPER PROMISES TO COMPLY WITH SECTION 272.

69. BellSouth has suggested that any section 272 compliance problems that it experiences will be uncovered and quickly rectified by either internal or external audits. See Cochran Aff., ¶26. BellSouth's compliance history, however, demonstrates that neither internal nor external audits will ensure that BellSouth will comply with section 272, and give substantial reason to doubt BellSouth's current paper promises of future compliance.

³⁶ (...continued)

employee of BSLD is currently, or will be, simultaneously an officer, director, or employee of [BellSouth].").

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70. For example, the results of a joint federal and state audit of BellSouth's dealings with its affiliates³⁷ gives little reason to credit BellSouth's current promises that it will act in compliance with section 272. The Joint Audit, undertaken on behalf of the Commission and the National Association of Regulatory Utility Commissioners, "attempted to evaluate whether cross-subsidy exists between [BellSouth's] regulated and non-regulated operations."³⁸

71. The audit team stated that BellSouth made it difficult for them to render an opinion regarding whether BellSouth was subsidizing nonregulated affiliates because of BellSouth's "consistent pattern of obstructionist behavior," which continued for at least eighteen months.³⁹ Furthermore, the audit team found that due to the lack of cooperation on the part of BellSouth that "many of the audit objectives were not fulfilled."⁴⁰

72. Similarly, in a related investigation of BellSouth's accounting practices, the Commission found numerous apparent violations by BellSouth of accounting rules and reporting requirements.⁴¹ In particular, the Commission found that:

³⁷ Regional Audit of BellSouth and Certain Affiliated Companies, Dec. 17, 1993 ("Joint Audit") (A copy of this audit is attached as Attachment 5 to my affidavit).

³⁸ Id. at 11 (Attachment 5).

³⁹ See id. ("obstructionist behavior" began in "May of 1992" and continued through at least December 1993).

⁴⁰ Id.

⁴¹ In the Matter of the BellSouth Operating Companies, Order to Show Cause, 10 FCC Rcd 5637 (1995) ("Order to Show Cause") (Attached to this affidavit as Attachment 6). The Commission found numerous accounting irregularities including: (1) working capital violations; (2) jurisdictional separations violations; (3) misclassification of revenues; and (4) internal control failure including inadequate documentation to support accounting adjustments.

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"The independent auditor's findings that we address here involve the misstatement or miscalculation of some \$6.2 million of interstate costs and revenues for the period from January 1988 through March 1989. . . . The seriousness of the misstatements is compounded here not only because of the net impact and the extent of understatements and overstatements, but also because of the scope and number of the errors or apparent violations, and the fact that they may have continued to the date of this Order to Show Cause. The findings reveal the BellSouth carriers' apparent failure to maintain their accounts, records, and memoranda in the manner prescribed by the Commission. To the extent that this conduct has continued, it must seriously undermine the Commission's confidence that BellSouth's accounts accurately reflect Commission-mandated accounting practices and reveal the true and lawful costs of BellSouth's interstate services."⁴²

On November 1, 1996, more than eight years after the initial violations, the Commission issued a Consent Decree in which BellSouth agreed to appropriate corrective actions, including an independent audit of its internal accounting controls.⁴³

73. The results of these federal and state audits demonstrate that the Commission should give little weight to BellSouth's paper promises that 272 problems will be identified and quickly rectified by internal and external audits.

74. This history shows BellSouth's willingness and ability to engage in obstructionist behavior to delay regulatory proceedings and judgements until its anticompetitive behavior has irrevocably altered the marketplace. Moreover, this history demonstrates that BellSouth's limited internal audit processes cannot be relied upon to promptly discover or rectify any problems that may emerge. The "past and present behavior of [BellSouth is] the best indicator of whether it will carry out the requested authorization in compliance with the

⁴² Order to Show Cause at 5638 (emphasis added).

⁴³ In the Matter of the BellSouth Operating Companies, Consent Decree Order 11 FCC Rcd 14803 (1996) ("Consent Decree Order") (Attached to this affidavit as Attachment 7).

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requirements of section 272." Ameritech Michigan Order, ¶ 347. This past and present behavior demonstrate that until BellSouth brings forth tangible evidence of procedures or systems in place to protect against section 272 violations, the Commission cannot find that BellSouth will meet its obligations under section 272.

IX. BELLSOUTH'S PLANNED USE OF CPNI UNDER SECTION 222 CANNOT BE SQUARED WITH THE NONDISCRIMINATION REQUIREMENTS OF SECTION 272.

75. BellSouth intends to share CPNI with BSLD to the full extent allowed under the Commission's CPNI Order regarding Section 222 of the Act.⁴⁴ See Varner Aff. ¶¶ 232, 229. In the Non-Accounting Safeguards Order, the Commission held that CPNI is subject to the nondiscrimination requirements of Section 272 because "the term 'information' [in Section 272] includes, but is not limited to, CPNI." The CPNI Order, however, reversed this decision, holding instead "that section 272 imposes no additional CPNI requirements of BOCs' sharing of CPNI with their section 272 affiliates." CPNI Order ¶ 169. AT&T Corp. has requested reconsideration of this aspect of the CPNI Order, which authorizes BOCs to discriminate in favor of their Section 272 affiliates in violation of the plain language and intent of Section 272's nondiscrimination requirements.

76. The CPNI Order authorizes discriminatory treatment in favor of the BOCs' Section 272 affiliates that puts competing IXC's at a substantial competitive disadvantage. For

⁴⁴ Implementation of the Telecommunications Act of 1996, Telecommunications Carriers' use of Customer Proprietary Network Information and Other Customer Information, CC Docket No. 96-115, Second Report And Order And Further Notice Of Proposed Rulemaking (rel. Feb. 26, 1998 ("CPNI Order").

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example, under the CPNI Order, a BOC may provide its Section 272 affiliate with CPNI information, without affirmative written customer approval, where the BOC is providing local service to the customer and the Section 272 affiliate is providing long distance service to the customer. See CPNI Order ¶¶ 158-169. By contrast, where the BOC is providing local service to a customer and an unaffiliated carrier provides long distance service, the unaffiliated carrier must obtain the affirmative written consent of the customer to obtain the local CPNI.

77. For these reasons, BellSouth and BSLD should not be found in compliance with Section 272 without having committed to provide BSLD and CLECs with equal access to its CPNI.

X. BELL SOUTH'S MARKETING PLANS VIOLATE EQUAL ACCESS PRINCIPLES AND GO BEYOND WHAT IS AUTHORIZED IN SECTION 272(g).

78. As in its prior applications before this Commission, BellSouth states that it intends to recommend BSLD long distance service at the outset of inbound calls for new service, while offering to read a random list of other available IXC's "if requested" by the caller. Varner Aff. ¶ 248 at 91. BellSouth proposes the following marketing script for inbound calls from customers requesting new service or a change in existing service:

"You have many companies to choose from to provide your long distance service. I can read from a list the companies available for selection, however, I'd like to recommend BellSouth Long Distance." Id. ¶ 249 at 92.

79. As the Commission found in the Ameritech Michigan Order, which considered a virtually identical marketing proposal, the practice of immediately steering inbound callers for new service to the Section 272 affiliate's long-distance service is "inconsistent on its

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face" with the equal access requirements mandated by section 251(g) and would allow BOCs "to gain an unfair advantage over other interexchange carriers." Ameritech Michigan Order ¶ 376.

80. The Commission's abrupt reversal of this decision in the BellSouth South Carolina Order⁴⁵ cannot be justified. As the Ameritech Michigan Order and the Non-Accounting Safeguards Order properly found, the Act mandates, in Section 251(g), that existing equal access rules remain in full effect and require BOCs to neutrally advise inbound callers of their right to select a long-distance carrier of their choice. Ameritech Michigan Order ¶ 375; Non-Accounting Safeguards Order ¶ 292. These equal access requirements serve to limit the BOCs' ability to leverage their market power arising from their bottleneck control of local exchange facilities improperly to favor one IXC over another.⁴⁶ By recommending BSLD's service even before

⁴⁵ Memorandum Opinion and Order, Application of BellSouth Corporation, et al., Pursuant to Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, InterLATA Services In South Carolina, FCC 97-418, CC Docket No. 97-208 (rel. December 24, 1997) ("BellSouth South Carolina Order").

⁴⁶ Indeed, a concern over the ability of BOCs to leverage and abuse their market power in this context has caused a California PUC ALJ to recommend imposing greater restrictions on joint-marketing than are required by the Ameritech Michigan Order. The ALJ's recommendation, still under consideration by the California Commission, directs that if a customer expressed an interest in hearing about the affiliate's interLATA service, then his call would be transferred to a special marketing group within the BOC, separate and apart from the customer service representatives responsible for taking new service calls. See Application of Pacific Bell Communications for a Certificate of Public Convenience and Necessity to Provide InterLATA, IntraLATA and Local Exchange Telecommunications Service Within the State of California, Calif. PUC, A.96-03-007, at 36-41 (May 5, 1997). Separating the marketing of the affiliate's services in this fashion would reduce the risk that BOC representatives would engage in unfair marketing practices, including the discriminatory use of CPNI, and would aid in identifying the costs of such activities so as to deter subsidization of the affiliate.

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asking callers whether they already know what long distance carrier they wished to select, BellSouth's proposal baldly violates these equal access requirements.⁴⁷

81. At a minimum, if equal access is to have any continued meaning, BOCs must be required to follow the joint-marketing procedures dictated by the Ameritech Michigan Order. BOCs at the very least, therefore, must be required -- before engaging in any marketing of their affiliate's services -- to advise inbound callers that they have a choice of long-distance carriers and to offer to read a neutral list of these carriers. If the caller selects a long-distance carrier, then no marketing effort to change the caller's mind should be allowed, as such tactics could lead callers to believe that they must choose the BOC's affiliate as an IXC in order to forestall delay or mishandling of their local service requests.

82. An even more modest alternative -- which although not fully implementing equal access requirements would at least give callers an opportunity to select an IXC of their choice before being subjected to BOC marketing -- would be to require that BOCs postpone their marketing during inbound calls until after they have advised customers they have a choice of IXCs for long-distance service, and have asked customers whether they have selected an IXC. If at this point the customer selects a particular IXC, then no marketing would be permitted. This approach would eliminate the need to recite a listing of available

⁴⁷ As the ALJ for the California PUC has found: "The equal access requirement is an empty formalism if Pacific Bell can satisfy it by simply referring to 'many choices,' and then describing its affiliate's long distance service in detail." Application of Pacific Bell Communications for a Certificate of Public Convenience and Necessity to Provide InterLATA, IntraLATA and Local Exchange Telecommunications Service Within the State of California, Calif. PUC, A.96-03-007, at 36-41 (May 5, 1997) (ALJ decision).

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IXCs, unless requested by the customer. Such an alternative would impose no added burdens on BOCs, and would preserve some important aspects of the equal access regime by requiring that the initial customer interaction not favor a particular IXC.

83. Such continued application of equal access principles at the outset of the presubscription process -- as required by section 251(g) -- imposes no new or undue burden on BOCs. BOCs simply would continue to follow the well-known procedures already in place to make the required equal access disclosures.⁴⁸

84. For these reasons, the Commission should reassert the equal access principles identified in the Non-Accounting Safeguards Order and the Ameritech Michigan Order -- and mandated by section 251(g) -- and find that BellSouth's marketing proposal for inbound calls violates these equal access requirements.

85. In addition to running afoul of its equal access obligations, BellSouth's marketing plans also appear to fall outside the scope of section 272(g). BellSouth states that it intends to assist BSLD in the "development and creation of packages of local and long distance services offered on an integrated basis," and that it views such services as within the ambit of Section 272(g) (relieving them of the nondiscrimination requirements of section 272(c)). See

⁴⁸ Contrary to previous complaints registered by BOCs, AT&T is not aware of a single BOC that currently feels compelled by equal access requirements to list each and every available IXC before accepting an IXC selection from a customer. Instead, BOCs meet the equal access requirements in different ways, with some reading substantially truncated lists of available IXCs (which lists periodically change), and others reading more lengthy lists, but allowing the customer to interrupt at any time with a selection. To my knowledge, BOCs typically only will read such a list of IXCs when a caller does not already have an IXC in mind.

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Cochran Aff. ¶ 30. In the Non-Accounting Safeguards Order, however, the Commission described the scope of section 272(g) as follows:

Some of the activities identified by the parties appear to fall clearly within the scope of section 272(g)(3) and hence would be excluded from the section 272(c) nondiscrimination requirements. For example, activities such as customer inquiries, sales functions, and ordering, appear to involve only the marketing and sale of a section 272 affiliate's services, as permitted by section 272(g). Other activities identified by the parties, however, appear to be beyond the scope of section 272(g), because they may involve BOC participation in the planning, design, and development of a section 272 affiliate's offerings. In our view, such activities are not covered by the section 272(g) exception to the BOC's nondiscrimination obligations.

Non-Accounting Safeguards Order ¶ 296 (emphasis added).

86. The coordinated "development and creation" of packages of service identified in the Cochran Affidavit, although vaguely described, appears to involve BellSouth in the very type of "planning, design, and development" of BSLD's offerings that the Commission identified as outside the scope of section 272(g). And because these services are not "joint marketing" within the meaning of section 272(g), they can be provided only if they are made available on the same terms to other IXC's.⁴⁹ No such showing has been attempted by BellSouth. On this record, therefore, this Commission cannot conclude that BellSouth's anticipated

⁴⁹ BellSouth sought reconsideration of the Non-Accounting Safeguards Order on the ground that the Commission, in the above-quoted passage, defined the "marketing" functions permitted by section 272(g) too narrowly, claiming that the definition should include "product development and strategy." See BellSouth Petition For Reconsideration, CC Doc. No. 96-149, at 7-10. BellSouth thus agrees that the coordinated "development and creation" of packages of services described in the Cochran Affidavit are not within the Commission's definition of "marketing" under section 272(g).